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DEMOCRATIC REFORM IN UKRAINE
DOES WESTERN POLICY UNDERMINE THE CHANCES FOR
SUCCESS?

by

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A Research Report Submitted To The Faculty

In Fulfillment Of The Curriculum Requirement

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Abstract

Successful economic reform and the transition to a free-market economy under a stable political system is the key to Ukraine's successful road to a new democratic beginning. Western assistance should primarily serve in an advisory role to stabilize the Ukrainian government, establish a viable rule of law, rudimentary representative government, and a system to protect individual and investment capital followed by direct investment and joint economic ventures with Ukrainian companies.

This paper proposes a sequentially phased transformation model which encourages Ukraine's leaders to concentrate their efforts on first building a stable government, although not necessarily a democracy, and then focus on meaningful economic reforms to establish a solid economy with free market principles. In the long term, free-market economic principles will undermine an authoritarian government and foster the introduction of a democratic government. Current Western efforts supporting simultaneous political and economic reform are inconsistent with Ukraine's cultural and historical past and undermine democratic and economic reform.

Chapter 1

Introduction

Successful economic reform and the transition to a free-market economy is the key to Ukraine's successful road to a new democratic beginning. Failure to make the successful transition to a free-market economy will derail democratization. But a successful transition to a free-market economy is by no means assured given the significant political in-fighting and minority ethnic interests that are disillusioned by the slow progress towards democratization and the failure to realize a better way of life. The transition will also be delayed as a result of a lack of a clear understanding of the desired result and a lack of experience with the processes to achieve them. Ukraine's transition to a free market economy will take longer than originally expected and will precede the process of democratization that will eventually result in representative government. Western assistance should primarily serve in an advisory role to stabilize the Ukrainian government, establish a viable rule of law, a rudimentary representative government, and a system to protect individual and investment capital. The hope is to create an atmosphere for direct investment and joint economic ventures with Ukrainian companies.

The premise of this paper is that the initial path chosen by Ukraine—a simultaneous process of political and economic reform—is impeding Ukraine's transition to democracy. Similar to the other states of the Soviet Union (FSU), Ukraine cannot seriously approach

reforms of this magnitude and anticipate a successful transition to a free market economy and democratic form of government without adequate preparation. Now that Ukraine's transition is mired in political infighting and economic chaos, it is essential for them to concentrate their energies on building a temporarily stable government, although not necessarily a democracy, and then focus on meaningful economic reforms to establish a solid economy with free market principles. That is the key to their successful transition. Only then can Ukraine concentrate on building a democratic society.

The proposition in this paper is that Ukraine's road to democracy should be a three step process. The first step should focus on government stability. The second step should focus on free-market economic reform and the associated development of an economic middle class. The third step is the development of a western style democracy which will lead to a logical and inevitable progression toward free-market reform. Free-market economics and development of a middle class will undermine the government developed in the first stage, which is likely to be authoritarian, and will undermine it as a result of its inherent economic and individual-oriented principles.

This proposal is consistent with Ukraine's cultural and historical inclination to seek out or develop a strong center of power during times of weakness or distress. It also is consistent with the structure, influence, and omnipresent guidance of the Russian Orthodox Church, which continues to exert significant influence in Ukrainian political and social life. Further, this proposed model of transformation and the resulting social and political stability, will be shown to be consistent with Ukraine's recent past experience under communist rule and its association with Russia. It is this consistency with Ukraine's historical, cultural, religious, and social past that gives this proposed transition model the

opportunity to stabilize Ukraine's current political and social unrest and provide it with the best hope for a successful political and economic transformation.

Chapter 2

Possibilities for Development

Ukraine's future, much like Russia's, will be critically determined by what happens over the next several years. There are several possibilities for political and economic development.¹ The first possibility is a continuation of the present disorder with an ensuing simultaneous economic and political collapse with resulting widespread civil disorder. This condition likely leads to a dictatorship to restore both the political and economic order. The authoritarian government would reestablish essential civil sector services, while the military maintains a defensive posture restoring domestic order. Democratization and economic reform would be halted for the near term.

The second possibility is one of a lack of economic and political progress towards reform. In this case, the country muddles forward making sluggish economic reforms amidst a corrupt political system lacking a viable legal structure. The government becomes mired in political infighting with ethnic groups and favoritism among the former Apparatchik. The economy operates at a low rate of efficiency and the bulk of day-to-day living is conducted in a shadow black market system with bartering of goods and services. Progress toward a free market economy and a democracy is lethargic with occasional setbacks.

In the third case the government takes the initiative to establish a firm rule of law, and seeing some retrenchment some of previous democratic gains. Both the military and the former communist party Apparatchik collaborate to form a stable central government, primarily authoritarian, with limited political freedoms. Subsequent efforts are made by the government to introduce free-market economics together with a continuation of the slow privatization of state industries. Many social services are restored although at reduced levels from the former Soviet period. Democratic reform of the authoritarian government follows free-market reform.

Of these three possibilities, I propose that the latter is not only the most likely to occur, but is also the most likely to succeed. What follows from this reasoning is a proposed model to guide Ukraine's transition first through free-market economic reform and a framework for subsequent democratic reform.

This paper proposes a transition model which is consistent not only with Ukraine's historical and cultural past but also with the progress of the initial Kravchuk and Kuchma governments efforts since Ukraine declared independence from the Soviet Union in 1991. It also argues that even though this transition model is appropriate for Ukraine, and is its most efficient route to both democratization and economic reform, it is likely to meet with significant western disapproval, particularly in its initial stages. Western nations, interested in promoting the development of a democratic government in Ukraine, are likely to be frustrated with the initial form of government that develops in the first phase, yet will need to accept and support a government short of democracy during the initial nation-building process. The most likely western response to the form of government that develops in this first stage will be disapproval and some withholding of aid. Disapproval which stems from

a lack of democratic principles early in the process will actually delay implementation of a democratic government in the long term. The West needs to take the long view toward democratization in Ukraine and not get sidetracked on short-term disagreements with the interim form of government in the first phase of the transition model.²

Only with a clearly defined and orderly effort focusing first on national stability, then on building a free market economy and development of an associated middle class, and lastly on a democratic form government, is Ukraine likely to achieve long-term economic success, political stability, and a better way of life for its people as well as acceptance into the international community. However, this will take time and ideological and financial commitment that the West, in light of its limited interests, transitory interest span, and available funds, may not be willing to commit. Further complicating matters is both the Russian and Ukrainian people's long cultural tradition and unique sense of national destiny which complicates Western efforts to assist in reform, if they are seen to be imposed from the outside. At best, the West will be a facilitator for Ukraine's own journey down the road to economic reform and democracy.

Notes

¹For an excellent discussion of Ukraine's, as well as Russia's, future alternatives, see Daniel Yergin and Thane Gustafsen, *Russia 2010 and What it Means for the World*, Random House, 1993.

²Acceptance of an initial form of government, short of democracy, clearly has its limits. It is important, however, that these limits be all encompassing and tolerant. Western financial and political influence can insure that a despot or dictator like Stalin does not arise. This paper argues that the likely form of government will be authoritarian and that human rights and individual freedoms in this initial phase be measured against an Eastern European standard rather than an American standard.

Chapter 3

Models for Democratization in Ukraine

Before we examine events in Ukraine, let us define democracy as it applies there. The fundamental characteristics of a rudimentary democracy include freedom of speech, the ability of the individual to redress grievances through the government and an independent judicial system, freedom of assembly, the right to form political parties, and regular elections in which all adults can participate to choose candidates for legislative and executive positions.¹

Much has been made about the several models or transitional routes from an authoritarian communist, state-controlled, centrally planned economy to a democratic government and a free-market economy. These several "roads to democracy" have been typically categorized into several models. One is the China model: a system of controlled economic transition to a free market system while maintaining the central communist state government. Another is the Russian model in which both the economic and political systems undergo simultaneous transformation. Yet another is the Ukrainian model of slow, controlled economic privatization coupled with simultaneous political and free market reform. There are many additional models that could be studied, whether it is Poland's "shock" transformation, East Germany's assimilation into West Germany, or any variant in between.

Beyond these rudimentary ideas about democracy, however, it is important for the West not to dictate the details of any particular system based on a particular western democratic experience. Ukraine's enhanced historical awareness, as the site of the foundation of the modern Russian state in 988 AD, and its historical cultural tendency to call for a strong central authority during times of weakness and distress culminating in its recent 70 years under Soviet communistic domination, have given it a social and political experience that will not easily lend itself to the current form of western democracy. The current western democratic paradigms should not impede the willingness of the industrial democracies to support these unique political systems.²

It is important to note that few of these former Soviet Union or Warsaw Pact countries actually *chose* their method of transformation. In reality, the selected road to reform was determined, among others, by their varying levels of domestic economic and political dissatisfaction, proximity to the West, and the intensity to which they felt that the communist system had exploited, betrayed, or let them down. There have been few conscious decisions to initially choose their model of reform as each started down this road, with the exception perhaps of Gorbachev's initial reforms in the late 1980s. Even then, however, his efforts rapidly got out of hand and exceeded his expectations. Boris Yeltsin's nationalistic appeals to the Russian people and support for the fledgling democracy fanned dissension and early movements toward democracy. His efforts did not so much create a democratic movement as they influenced a movement gaining momentum toward a more democratic society.

Thus as one talks about the models to democratic transformation, it is important to understand that each of these countries did not have a central steering committee that

planned from the beginning each step in the evolution of their social and governmental structure. Rather, the initial model chosen for them was shaped predominantly by the circumstances of the moment. Given their varying lack of control at the outset, however, each has had the opportunity and ability to alter, shape, and influence the road their initial model has led them. It is this ability to modify and tailor their initial efforts that is the best indicator of long-term success.

In the case of Ukraine, the Kravchuk and Kuchma governments have wrestled with the model chosen for them and have had the best, albeit limited, success of the former Soviet states. This slower and more controlled transition will have benefits in the long run, but a lack of focus and experience, coupled with domestic pressure from an increasingly dissatisfied population, may derail their efforts toward democratization. In order to capitalize on their initial success, Ukraine needs to concentrate its efforts on stability because this will enhance its chances for success of privatization and economic transition. As with other countries around the world, democracy in Ukraine will necessarily be home grown.

Notes

¹Carol J. Lancaster, *United States and Africa: Into the Twenty-First Century*, Overseas Development Council Policy Essay No. 7 (Washington, DC: Overseas Development Council, 1993), 51.

²Japan, although clearly a western style democracy is excluded here from applicability due to significant cultural differences. One important difference is that Japan's government was established by the United States after 1945.

Chapter 4

A Proposed Transition Model for Ukraine

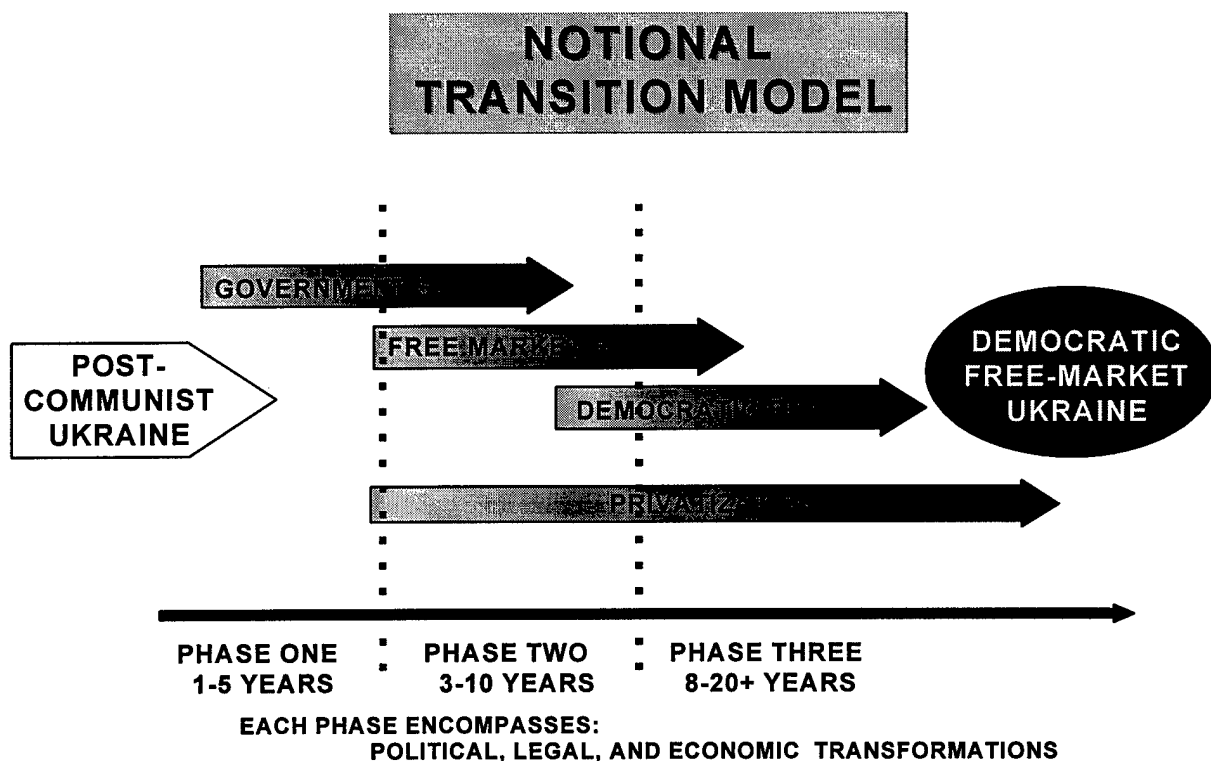
If Ukraine is to progress economically, compete in world markets, develop a representative government compatible with its traditional past, and establish human rights, it must systematically attack not the symptoms of its current problems but rather the root causes. It is important that western assistance support these efforts with this long-term goal in mind. The current state of affairs in Ukraine is one of deterioration in the political, economic, and social order.¹ Although an international measure of stability has been introduced with the agreement to remove all nuclear weapons from the country, significant political infighting and an inability to achieve governmental consensus threaten the government's ability to manage the ongoing privatization program. In a rapidly changing and uncertain environment, policy initiatives to date have tended to be piecemeal and reactive in nature.² The root cause of Ukraine's current deteriorating political and economic instability lies in its inability to achieve political consensus among the various ethnic-based political factions coupled with an dependence on outside sources for natural resources. Ukraine's previous economic development and resulting political stability was facilitated as a result of years of interdependence with Russia.

If growing chaos rules a country and the lack of political and physical infrastructure means that people are starving, then efforts should focus on attacking the root cause of the

troubles, which is governmental stability. Similarly, if a strong central authority exists, providing stability, but the economy is crippled through central state mismanagement, the focus should be on introducing decentralized free-market economic principles. Given the current state of political and economic instability in Ukraine, the sequence that highlights the most promising road to a representative form of government includes first establishing a stable government or central authority, followed by free market economic reforms and the rise of the middle class, and finally a representative democratic form of government.

This proposed model represents a series of governmental, economic, and legal reforms that fall into three distinct phases which are applicable to many states of the former Soviet Union. As a series of phases, it may be entered at any point or phase. For example, states which already possess a stable central government, characterized by a rule of law, will enter the model later, such as at the phase of the introduction of a free market economy, as in the case of China. Similarly, authoritarian states with fledgling free-market economies, such as Cuba, would enter the model well into the free market economy phase. This sequence of events—government stability; introduction of a free market economy; and democratization—occur in overlapping phases.

This sequential phasing is better illustrated in the diagram below.



Lt Col James S. Davis, April 1996

Figure 1. Notional Transition Model

Phase One—Governmental Stability

Governmental stability must occur before either economic or democratic reforms. The premature introduction of political democracy, which is the Clinton Administration's ultimate goal, will diminish a nation's capacity to cope with its internal and external economic demands.³ The decision to support a stable form of central authority, almost regardless of its form, is a crucial one. Whether a country is emerging from its colonial past, embroiled in civil war, or wallowing in political corruption and organized crime, it must focus on providing a stable order and predictability within the government and the society.

The focus of this first stage is to stabilize the central government's ability to carry out public functions and services in response to basic social and economic needs, thus helping to solve some of the root problems that inhibit the development of stable democratic institutions. This first stage of governmental stability is characterized by the rule of law ensuring the safety of nationals and foreigners, basic protection of property as well as domestic and foreign investment capital, increased control over factional struggle, basic human rights, identification as a nation-state, and the ability to act in the international system. Additionally, this first phase should codify a predictable legal system with an associated predictable level of corruption.

Governmental stability is essential to providing a predictable level of social order to encourage third party interaction within the society. Governmental stability is further necessary to ensure that a basic low-level social safety net is in place to provide a minimal subsistence level for the population as well as the security of nuclear weapons. This stability will provide the prerequisite security for follow-on commercial enterprises development. Together, these will provide the basis for governmental stability and basic social order.

An early democracy in Ukraine may not be up to the task of solving its security, governmental, economic and social problems. It may even be destabilizing. Governmental stability is important to provide the foundation upon which to build a free-market economy. The form of that government is not critical. The role of the military in this first stage may not be unlike that with which it is currently tasked.

Finally, it is important that we avoid applying US standards for individual freedom and self-actualization or which place too much emphasis on human rights early on.

Premature focus on the end result, without establishing the foundation, will destabilize the developing nation-state and derail the process of democratization. Stabilization of the government, control of corruption, and the protection of domestic and foreign investment provide the essential rudiments for the next step, which is the introduction of a basic free-market economy.

Phase Two—Introduction of Free-Market Economy

Following initial governmental stability, the state can progress into the second phase: introduction of a basic free-market economy. The focus of this phase includes support for domestic individual and corporate investment, assistance in trade mechanism development for both the domestic and international market, and joint economic ventures coupled with a viable business banking system. This phase is characterized by elimination of price controls and subsidies, and an end of collectivization as well as a concerted effort on infrastructure development. Privatization of state controlled industries begins and continues throughout the democratization process.⁴

Once there is basic governmental stability, then the development of a free-market economy will do more to promote democracy and human rights than decrees from a governmental agency. It must develop the rudiments of a free market economy characterized by the rise of a middle class. Individual entrepreneurship, private investment, and bilateral foreign trade are all antithetical to a closed, authoritarian, economic, political and social system. A free-market based system in which the individual has a key stake in the future, where rewards are based on individual effort, and where interaction with societies outside the state, has the potential to bring down authoritarian rule.⁵

The current economic liberalization in China will be yet another useful test of this model of economic reform before political reform. It will be useful to see whether the economic liberalization that is already leading to political reform, albeit only in China's southern region, will eventually undermine the Chinese ruling elite.

It was the economic forces of a shock transformation from a command economy to the initial stages of a free-market economy, and then an attempt to return to the command system, that led to the complete unraveling of the Soviet state.⁶ This self-destructive future can be prevented in Ukraine. Given that it proceeds with the maintenance of a stable central government, consistent with Ukraine's recent colonial past, Ukraine can proceed with free-market reforms. After free-market reforms take effect, those same forces will be integral in the development of a middle-class, transformation of the governmental system into the next stage of democratization, and the development of a democracy consistent with Ukraine's unique historical and cultural past.

Phase Three—Development of Democratic Principles

Lastly, with a stable government in place, a growing middle class, and a developing free market economy, Ukraine can fine tune its development of a democratic form of government that is unique to its cultural and historic past. This phase is initially characterized by the formation of stable political parties, freedom of the press, and an end of the one party state. Inevitably, the constitution will go through several revisions as the various political and ethnic factions balance power. Coupled with these reforms come multi-party elections and a stable democratic governing coalition. This state of the transformation model is the most difficult to predict as it will be determined by the

ongoing political, social, and economic pressures of the society. As indicated in the model, democratic reforms are not likely to occur until 8-10 years into the process and may take decades to accomplish. It is not until this final phase is reached that a representative government, which is more acceptable by western standards, is likely to appear.

The order of the reforms is important if the democratization process is to succeed, because initial government stability, almost regardless of its form, is the key to the quickest implementation of a fledgling free market economy and stability within the social structure. As free-market economy principles take hold, they will destabilize the authoritarian government that brought them about in favor of a more democratic one.

The West must have the patience to stay the course by supporting this initial government of stability, even though it may deviate significantly from the desired result. Disapproval of the initial form of government and subsequent withholding of aid will derail or significantly delay economic reform and subsequent democratization. Western support and aid during this critical period will ensure long-term progress toward the desired outcome of a democratic form of government.

Western Reluctance to Accept Model

The road to democracy proposed by this model will not be well received by the West because it advocates that Ukraine choose its own initial form of government. It not only requires initial acceptance of a government of stability that may not be consistent with western democratic ideals, but also raises the specter of a possible authoritarian government, in the image of the former Soviet Union and potential reemergence of a new form of the Cold War. Excessive emphasis on the democratic and human rights of the

individual, combined with the natural western impatience for a quick solution to any problem, will be contentious. Given Ukraine's historical background, the historical tendency of the people to seek out a strong ruler during periods of turmoil and their recent experience with the Soviet authoritarian government, it is unlikely that a democracy will initially develop. With the current political turmoil and significant economic problems, it is more likely that Ukraine will turn to its recent historical past to find short-term solutions. Given the West's proclivity to tie economic aid and assistance to an endorsement of the principles of the government in power, it is likely that they will withhold support and thereby delay reform. Events in the late 1980s show that a free market economy, by its very nature, tends to destabilize authoritarian governments.

There are, however, slightly different models for transition which describes each phase in Ukraine's transformation, and thereby provides insights into what would be accomplished in each phase (see Table 1).

Table 1. Ukraine's Post Communist Transformation

	Phase One: 1-5 years	Phase Two: 3-10 years	Phase Three: 5-15+ years
Political	Basic democracy, free press, end of one-party state	New constitution, elections, stable democratic governing coalition	Formation of stable parties
Legal	Elimination of state controls	Legal framework for business	Independent judiciary, full legal culture
Economic	Elimination of price controls and subsidies, end of collectivization	Banking system, small and middle-scale privatization	Large-scale privatization, entrepreneurial culture

Source: Adapted from Zbigniew Brzezinski, National Review, Autumn 1993 as published in *The Economist*, May 7th, 1994

The problem with this approach is its simultaneous economic, political, and economic reform, which requires the introduction of democracy in Phase One. Further, it fails to take into account Ukraine's historical and cultural legacy, both in its recent 70 years of association with the former Soviet Union and in its development as a culture over the past 1000 years. In contrast, the sequential transformation model proposed in this paper will work with any stable form of government because it will provide the necessary foundation for the introduction of a free-market economy.

Notes

¹International Monetary Fund, *Economic Review: Ukraine*, June 1992, Washington, DC, 8.

²*Ibid.*, 8.

³Earl Conteh-Morgan, "The Military and Human Rights in a Post-Cold War Africa," *Armed Forces and Society*, Vol 21, No. 1 (Fall 1994): 142.

⁴Although there will certainly be rudimentary privatization efforts occurring in Phase One, they will most likely be very limited in scale and are not the emphasis in that phase.

⁵This premise has yet to be shown, although there are many examples in the making. China is attempting economic reform while maintaining a socialist government. It remains to be seen whether the economic reforms there will destabilize the strong central government. Cuba also provides another example of a socialist regime that is attempting economic reform, particularly in the area of private enterprise, while maintaining a strong socialist government. Although Cuba is not as pure of an example as is China, each has the potential of validating this premise.

⁶Nicholas Chirovsky, "The Commonwealth of Independent States," *Ukrainian Quarterly* XLVIII, no. 4 (Winter 1992): 398.

Chapter 5

Initial Reform Goals

It is useful to review the process by which Ukraine made the transition to a nascent democracy because these events have determined progress toward democratization to date and will shape the future. The road to democracy in Ukraine started in 1985 with Mikhail Gorbachev's announcement of a new policy of perestroika. Through his subsequent new openness in glasnost and his eventual program of democratsia, Russia and the republics of the former Soviet Union started down a road for which they were little prepared. As the Soviet Union gradually disintegrated, the economic situation went from bad to worse. Gorbachev tried to save the Soviet Union for about three years but to no avail. He started some reforms toward a free market, but then he reverted to central planning. Without much success, the Supreme Soviet of the USSR was called into session several times. Finally, failing to hold the union together, the individual republics of the USSR began to proclaim sovereignty and independence in a process that included Ukraine.¹ Growing nationalist sentiment and opposition to Soviet rule culminated in the Declaration of Sovereignty on July 16, 1990 and the Declaration of Independence on August 24, 1991.² On December 1, 1991, Ukraine's referendum on independence resulted in a 90 percent endorsement for independence with simultaneous presidential elections, which led to the election of Leonid Kravchuk.³

When Boris Yeltsin announced in 1992 that Russia would make the transition to a new way of life in a market economy, neither he nor the members of the former Soviet Union understood the long-term implications of such changes. They had no experience with a free market economy and democracy. Soviet tradition for the past several hundred years was that of a strong authoritarian government, either through conquering foreigners, the Czars, or the Communist Party. Democracy and a free market economy served as a rallying cry for a tired and bankrupt society with an ideology and government that had failed them. The universal reaction throughout the former Soviet Union states, including Ukraine, was a popular expression of renewed optimism and hope for a better way of life without having a clear idea of what that new way would be or how they would get there. Many felt that the West would embrace them with economic support and thereby accelerate the process of transition. But, it simply did not happen, largely because the previous seventy years of communist-style implementation had deprived them of the necessary tools to create a market economy, as well as the perspective that is necessary to develop a free-market economy.

Initial Political Goals

The initial goals of political reform were quite limited. President Kravchuk maintained power with former Communist Party *apparatchiks* who formed an alliance with selected nationalists. He initially maintained a centrist, consensus-building profile with a conservative economic reform program. Large numbers of communists and independent candidates in the government prevented the implementation of a coherent reform program. Unrest has resulted from the reluctance to devolve power, particularly among the pro-

Russian sympathizers, resulting in political instability. Democracy, as Kravchuk saw it, was primarily a focus on individual freedom and national self-determination. In his I have a Dream speech of May 1992, he stated that Living in peace is our most important goal. He argued that Ukraine would work to achieve that goal through reverence for the individual, respect for ethnic communities, and an unwavering regard for the inviolability and integrity of nations.⁴ From the early days of the Kravchuk government (1991-1994), he steadfastly argued that Ukraine was sovereign and unequal among other states in that regard, and that no member of the CIS should impose its will upon another. This was quite different from the Russian view of the CIS as a new way for organizing Russian hegemony of the former USSR. This contrast of views set the initial stage for the Ukrainian-Russian Cold War and Ukraine's subsequent political development.

Initial Economic Goals

Immediately following the declaration of independence, Kravchuk announced an initial plan for economic reform. His first step as president was to privatize the economy and transfer state property to the people, as promised during the election campaign. His plan pledged that every citizen of Ukraine will have the opportunity to acquire means of production...and land with the help of relevant stocks and shares, which guarantee the right of free acquisition of the property subject to privatization.⁵ He also announced the replacement of the Russian ruble with the Ukrainian coupon to stop the whole-scale Russian plundering of Ukraine.

The privatization of the economy plan was a two-stage program. The first stage of privatization, the so-called small-scale privatization, which involved small businesses, light

industry, and the food industry, was planned for 1992-1993. The second stage was privatization of heavy industry, which was scheduled to take place in 1994-1995. Initial planning for the distribution of land was done to encourage people to work and gain popular support.⁶ The government plan further called for establishment of a ministry of privatization, a state property fund, as well as numerous committees and commissions on privatization. Denationalization was the key to economic reform.

Notes

¹O. Chabariivskyi, "A Deepening Crisis in the CIS," *The Ukrainian Review* XL, no. 4 (Winter 1992): 7.

²"Ukraine—Country Profile," *Jane's Sentinel*, 1994, 5.

³*Ibid.*, 5.

⁴Leonid Kravchuk, "I Have a Dream," *Ukrainian Quarterly* XLVIII, no. 1 (Winter 1992): 350.

⁵Leonid Kravchuk, "Who Had Nothing . . . Will Have Nothing," *The Ukrainian Review* XL, no.1 (Spring 1991): 82.

⁶*Ibid.*, 82.

Chapter 6

Current Political and Economic Realities

The current Ukraine president, Leonid Kuchma, is determined to turn the economy around, but faces many harsh realities. There is significant disillusionment with economic reform. The expected significant increases in the standard of living have failed to materialize. Initial attempts at economic reform were met with hyper-inflation with *monthly* inflation rates of 833 percent in 1993, and 72 percent in 1994. These have been reduced to only 6 percent by July 1995.¹ While retail goods are available in adequate quantities for those with the money to pay extremely high prices, prices for most consumer goods are well outside the purchasing power of the average citizen. Military officers haven't been paid in months, unemployment is climbing, and industrial utilization is plummeting. President Kuchma's appointment of a fervent advocate of free markets, Viktor Pynzenyk, as the first vice premier was an effort to push privatization. However, he suffered a setback when Pynzenyk, representing the last reformist element in the Cabinet of Ministers, resigned only a year later in July 1995.² There is a general feeling among the population that things will get worse before they get better.³ For example, Kiev's buildings are heated by a series of central heating plants. Its occupants have already been told to expect less heat this winter and for it to be turned on much later in the season.

Some inroads are being made to stabilize the government and the economy. To stimulate economic growth and investment, the top income tax has been slashed to 50 percent. Privatization, previously progressing at a snails pace, is now being pushed hard. The government is determined to sell most of its land, which, if done properly will trigger an agricultural boom. Ukraine has also put a social safety net in place, providing a level and coverage of benefits similar to the more affluent OECD countries.⁴

Slow Pace of Constitutional Developments

Political instability in Ukraine stems from economic weakness, pro-Russian nationalist sympathizers, and discontent with the performance of the ruling old-guard communists.⁵ The development of human rights, civil society, and political reforms are all proceeding slowly. Political parties and the independent media still exert only a small amount of influence on the population. Membership in political parties and civic groups is small and political activism is low. The old regime still exercises a large degree of influence over the population, particularly in rural areas, provincial towns, and within the economy and society.⁶ The draft constitution has elements consistent with UN, CSCE, Council of Europe values and the rule of law, such an independent judiciary and separation of powers. It has been criticized for not ensuring a clearer separation of powers, leaving too much room for government intrusion, having insufficient mechanisms for the protection of human rights, and for instituting an executive branch that is too strong.⁷

The black market is a topic that has received a great deal of attention not only in the western press, but also in Ukrainian papers. On the one hand, there is certainly significant criminal activity in the economy. Existing taxation rates, which complicate running a

legitimate business, can be as high as 100 percent of revenue. On the other hand, the involvement of the Mafiya may be overstated.⁸ It is difficult to separate money used to bribe a government official to facilitate paperwork in the legendary former Soviet Union bureaucracy from protection money to ensure that one's business doesn't get torched in the middle of the night. Clearly, there is payment for services that would be illegal by conventional western standards. It is important to remember that this has traditionally been a part of the culture of the states of the former Soviet Union and is not likely to be eliminated in the near future.⁹ It may be argued that organized crime in Ukraine provides a certain predictable order to a chaotic society in transition, although that order will certainly be destructive in the long run.

Compounding Ukraine's inability to reform its economy is a lack of expertise in running the basics of a free market economy: a national banking system, credit system, and a method for protecting venture capital and providing legal recourse for business disputes. In addition, there have never been traditions for individual incentive or taking economic risks. In addition, Ukraine suffers from a near total reliance on Russia for energy sources, trade, and technical expertise and constitutes a major limiting factor in free-market development.

Ukraine is in the early stages of getting its political house in order. High on its list of concerns is the Crimea, nuclear weapons, neutrality, the Black Sea fleet, energy, environmental clean-up, and infrastructure reconstruction, among others. There is also the contentious problem of the Russian ethnic minority, particularly in the eastern part of the country, that opposes most reforms and would prefer far closer ties with, if not dominance

by, Russia. And there was a resurgence of communists in the 1994 parliamentary elections that placed Kuchma in office as President.

Current Western Assistance Overview

Western assistance to Ukraine has come in many forms, from various sources, and with various strings attached. Since 1991, the US and the Ukraine have entered into a series of bilateral agreements designed to enhance economic, technical, environmental, and cultural cooperation. Most of this assistance, to the Ukraine as well as to the other newly independent states, has been tied to the *Freedom for Russia and Emerging Eurasian Democracies and Open Markets (FREEDOM) Support Act*, enacted in October 1992. In September 1993, the Clinton administration approved a new \$2.45-billion assistance package for Ukraine and the newly independent states.¹⁰ The primary focus of this legislation has been political and economic reform, as well as basic humanitarian needs. Most notably, in March 1994, President Clinton and Ukrainian President Kuchma reached agreement on an expanded economic package that will provide up to \$700 million to Ukraine: \$350 million in technical and humanitarian assistance in FY94 funds and \$350 million in Nunn-Lugar funds (FY 1992-95 funds) to assist with nuclear disarmament, non-proliferation programs, and industrial partnerships.¹¹ Additional aid has come in the form of \$72 million in energy sector grants for the purchase of natural gas for Ukraine's heating and electricity needs. From 1992 through September 1994, the U.S. had obligated about \$196 million in humanitarian assistance and \$201 million in technical assistance. The general view in both Russia and the Ukraine among civil and military individuals is that Western aid to date was misdirected and inadequate. In particular, Nunn-Lugar funds,

although advertised as aid to Ukraine, was in fact money spent in the United States, on US companies and advisors, and had little impact where it was needed. The money benefited primarily the US not Ukraine.

Current US Strategy

The current US National Strategy describes Ukraine as a state which will play a vital role in the transformation of Europe.¹² Ukraine lies in a strategic central location and is a linchpin of the new post-Cold War Europe. If Ukraine succeeds in its transformation to an independent, free-market state, it will pave the way for others aspiring to follow the same path and increase their chances for success. It is appropriate to support such a state politically, economically, and even militarily. U.S. foreign policy toward Ukraine should be coordinated toward these ends.

Equally vital is the U.S. interest in Ukraine's development into a stable, secure, independent, democratic and prosperous state.¹³ To achieve these goals, the Clinton administration urged the Ukrainian government to cooperate with the International Monetary Fund in initiating initial economic reforms. At the July 1994 G-7 summit, the U.S. pushed for a \$4-billion economic assistance package for Ukraine. Together with U.S. economic assistance packages, the U.S. is working to ensure Ukraine's successful transition to a free-market economy.¹⁴ Ukraine and the U.S. have dealt both with the problems of removal of nuclear weapons from Ukrainian soil as well as and Ukraine's decision to join NATO's Partnership for Peace program. It is particularly important for both nations to promote not only good U.S.—Ukrainian relations for the sake of future development, but also good Ukrainian-Russian relations as well, for the sake of Ukraine's

future as an independent country. There is no doubt that Ukrainian reform, as well as its very survival as an independent state, is closely tied to Russian political and democratic reform.¹⁵ Success or failure in Russia could clearly determine not only the fact of Ukraine, but also the fate of many other former Soviet states bordering Russia.

The issue then becomes one of ensuring that the aid packages, currently ongoing in Ukraine today, are working to further U.S. national interests as well as the long-term interests of Ukraine. A consistent and coordinated effort would further these goals. A misaligned assistance package operating independently of U.S. objectives could prove counter-productive to both U.S. and Ukrainian efforts. In 1993, then Prime Minister Kuchma warned, essentially [the threat to the survival of Ukraine] all comes down to one thing—the ravaged economy.¹⁶

As discussed earlier, Ukraine has yet to begin Phase One at this time. What the prevailing model fails to take into consideration is the impact on the potential survival of the Ukrainian state, economy, and people and ultimately the government during the first and second phases. Phase One holds clearly the most potential for disruption and turmoil in the society. This phase is characterized by a shortage of consumer goods and services, a relaxation of artificial state controlled prices, and a failure to be able to compete on the world market with an outdated industrial base and outdated infrastructure. Currently, Ukraine is experiencing many of these problems, including hyperinflation, widespread unemployment, and a plummeting GNP. How they cope with these problems and how the West intervenes will set the tone and determine the probability of success for Phase Two and Three.

Future western involvement in the process must evolve from a clear set of national interests in the area. Only from these national interests can the proper level and type of involvement be determined. The objectives of US policy toward Ukraine are the establishment of a stable, secure, independent, democratic, and prosperous country.¹⁷

Notes

¹"A Long Night is Coming to an End," *Business Week—International Edition*, July 3, 1995 via the Internet.

²"A Kuchma's First Move: A New Cabinet," *Transition*, Vol. 1 No. 13, 28 July 1995, 8.

³Author Interview in Kiev, Ukraine, September 1995.

⁴International Monetary Fund, *Economic Review: Ukraine*, June 1992, Washington, DC, 10.

⁵"Ukraine—Country Profile," *Jane's Sentinel*, 1994, 13.

⁶*Ibid.*, 8.

⁷"Ukraine—Country Profile," *Jane's Sentinel*, 1994, 8.

⁸The spelling here of Mafiya is the spelling used in the states of the former Soviet Union. I have chosen here to differentiate it from organized crime as it is known in the western world. Here it describes a pervasive organized element of crime, not unlike, but not connected to the traditional Sicilian crime syndicates.

⁹William C. Martel and Theodore C. Hailes, ed., *Air War College Studies in National Security*, Vol. 2, *Russia's Democratic Moment? Defining US Policy to Promote Democratic Opportunities in Russia*, (Maxwell AFB, AL: Air University Press, 1995), 137.

¹⁰"A Fact Sheet: U.S. Assistance to Ukraine," *U.S. Department of State Dispatch*, November 21, 1994, Vol 5, No. 47, 776.

¹¹*Ibid.*, 776.

¹²"A Fact Sheet: Ukraine's Future and the Future of Europe," *U.S. Department of State Dispatch*, November 21, 1994, Vol 5, No. 47, 773.

¹³*Ibid.*, 773.

¹⁴For an excellent overview and discussion of economic assistance to Ukraine, see *The A Promise of Assistance and the Stone of Sisyphus*, an unpublished research paper by Lt Col Robert L. Bivins, USAF, Air War College, Maxwell AFB, AL, 11 October 1995.

¹⁵"A Fact Sheet: Ukraine's Future and the Future of Europe," *U.S. Department of State Dispatch*, November 21, 1994, Vol 5, No. 47, 774.

¹⁶*Ibid.*

¹⁷Deputy Secretary of State, Strobe Talbott, Address before the Carnegie Endowment for International Peace, Washington, DC, November 18, 1994, *U.S. Department of State Dispatch*, November 21, 1994, 773-777.

Chapter 7

Potential Problems

Progression to a democracy, through the model described here, may occur quite differently or it may not occur at all. There are several alternative scenarios. In the first case, Ukraine may be forced into a closer alliance with, if not absorption into, Russia as a result of being unable to cope with its significant internal political divisions, inadequate resources to solve its economic problems, or the ability to control its military. It may find that the solution to its ethnic, economic, and security problems can be achieved through a close relationship or federation with Russia.

In the second case, Ukraine may seek to re-establish a Ukrainian-Russian federation as a result of a perceived military threat from NATO's eastward expansion. Should many of the Eastern European states of the former Soviet Union choose to join and be accepted into NATO, Ukraine may again find itself on the frontier, the origin of its name, a position it has become very familiar with over the past thousand years. Both Russia and Ukraine perceive NATO's planned eastward expansion as aggressive.¹ In a Ukrainian-Russian security agreement, Russia would get again get a buffer state and Ukraine would get security from Russia. In this case, as in the first case, Ukrainian progress toward democracy would be dependent on the rate and success of Russia's reform, with significantly reduced prospects for success.

A third alternative is continuation or variation of the status quo. In this case, Ukrainian President Leonid Kuchma continues to battle a divided parliament, making only limited progress toward democratization and free-market reforms. The Russian nationalists in the east and the ethnic Ukrainians in the west fail to agree on the need for either democratic or economic reforms and the country alternately aligns itself with, whomever will provide a better standard of living—either the reformers or the former communist regime.²

The model proposed here may meet with total failure, due to Ukraine's inability to steer through the reform process. Optimistic prospects for democracy in Ukraine are not universal and run to both extremes. The model proposed here is obviously more optimistic. Democracy is a people-oriented form of government that offers the potential for an improved way of life for the people of Ukraine. A free-market economy holds out the promise for a higher standard of living, keyed to an individual's effort. My expectation is that, although Ukraine will reform and initially develop along lines consistent with its historical past, it will break with those elements that have collectively bound its society together in favor of proactive individual efforts toward an improved standard of living and a more representative government.

Notes

¹Boris Tarasyuk, "A New Concept of European Security," *Transition*, 28 July 1995, 19.

²According to an USIA Opinion Analysis, A Ukraine, National Economy is Public's Main Concern, 13 January 1995, Ukraine is clearly divided. A representative sample of 2,028 residents of Ukraine aged 15 and over were asked the question, Which of the following [economies] do you favor for our country?, the answers were: Market Economy-21%, Mixed Economy-30%, Planned Economy-24%, with 25% A Don't know. Perhaps reflective of the recent decline in the standard of living, 45.6 % of the respondents favored a A Return to mostly state control of the economy while only 31% favored

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reducing the state's role. Perhaps the greatest source of concern comes out of the answer to the question, A How satisfied are you with the economic situation in Ukraine these days? Over 91% indicated dissatisfaction with only 0.5% answering Avery satisfied. Success or failure with economic reforms will be key to President Kuchma's continued mandate to lead the reform process.

Chapter 8

Conclusion

Ukraine's transition to a free market economy will necessarily progress through three major phases: building a stable governmental foundation, making the transition to a free market economy, and the continued development of a democratic form of government. A stable government based on a codified system of laws is necessary to protect both individual and fledgling corporate rights. The developing governmental foundation must provide a secure domestic society, a legitimate system of taxation, and a basis to protect both domestic capital and foreign investment. Only after a stable governmental foundation has been built can Ukraine progress to the initial transition to a free market economy. Without this stable foundation, both private and corporate property and domestic and international capital are at risk. As an editorial in *Forbes* magazine recently noted, We should encourage Kiev to continue slashing or eliminating those absurd tax rates, cutting out all import/export controls and get off the backs of the local business people. (It continues to propose that the government of Ukraine) set up a currency board to stabilize the value of its money. As long as property and capital are at risk, economic development will be stunted.¹ Current western shock therapy proponents who support simultaneous political and economic reform, are undermine the reform process and are counterproductive to Ukraine's democratic transformation.

As a result of inadequate preparation, little experience, and lack of a clear vision for the future, significant economic and democratic reforms are a long way off. In 1992, many in the former Soviet Union felt that the transition would complete itself in only a few years, but in reality, it may take more than 30 years. The domestic infrastructure of the states of the former Soviet Union is in a shamble, far worse than what the Germans found in the former East Germany. Entrepreneurship, independent action, production risk taking, capital leveraging, and investment are as yet unheard of. A taxation system that taxes \$1.26 on every dollar of revenue, and thus mandates two sets of books; widespread organized crime activity; a legal system with no effective way of protecting or adjudicating investment capital and property disputes; and an inability to even accurately measure current levels of economic activity, much less accurately reflect changes or trends in that economy—all have brought near economic and political gridlock to democratic reforms in the former Soviet Union.

In spite of this, it is important to remain optimistic that, with the proper focus and set of priorities, both economic and political reform will succeed in the former Soviet Union. Economic reform is far more complicated than they anticipated. The largest limiting factor is lack of experience. Economic reform has taken several wrong turns so far and will take many in the future. The West can best help both by showing the way through direct investment in joint ventures with Ukrainian companies. The West could also offer Ukraine meaningful trade agreements. All this could contribute not only to the growth of the middle class but could stabilize their fledgling economy and in the process build a sound democratic government.

The road to democracy I have described here is a variant of the China model, in which economic reform leads to democratic political reform. A critical element, which may be hard for western observers to accept, is the initial formation of a potentially non-democratic government in the first phase. While this phase may delay the human rights reforms that will eventually accompany democratic reforms, it will not obviate the need for short-term humanitarian aid. However, continued progress with economic reforms and the associated rise of the middle class offers the best assurance that democratic reforms will proceed, regardless of the initial form of government.

Notes

- ¹“Stop Stiffing Ukraine,” *Forbes*, December 5, 1994, 26.

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